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TAX LAW CHANGES IN 2004

SUMMARY

For many, 2004 will be remembered as the year the tax on food was eliminated. The bill that enacted this measure also removed the gross receipts tax on certain medical services and repealed the municipal credit to pay for the changes. This was certainly a highlight of the session in terms of legislative debate, public opinion and tax policy implications. However, as noted below, several other significant tax measures were also passed.

Tax on Food

Removal of the gross receipts tax on groceries has been widely discussed and debated in recent years. Laws 2004, Chapter 116 achieves that goal and represents the most significant narrowing of the gross receipts tax base in many years. Effective January 1, 2005, the legislation creates gross receipts tax deductions for receipts from food sold at retail food stores and for certain receipts of health care practitioners.

The definition of "retail food store" determines which establishments are eligible to deduct receipts from the sale of food. The new law defines retail food store as an establishment that sells food for home preparation and consumption and that meets the definition of retail food store for the purposes of the federal food stamp program. Pursuant to the program, an establishment must meet one of two tests to qualify as a retail food store. Either the establishment "must stock and offer a variety of foods on a continuous basis in each of the four staple food categories", e.g., breads/cereals, dairy products, fruits/vegetables and meat, fish and poultry, or if the establishment is a specialty store, e.g., a convenience store where the chief business is sale of gasoline, it must attribute "50 percent or more of its gross retail sales to staple foods".

Since a retail food store can deduct receipts from the sale of food, the definition of "food" is also pivotal to an understanding of the gross receipts tax deduction. The new law defines food as any food or food product for home consumption as defined by the federal food stamp program. The definition includes most staple grocery food items and cold prepared foods packaged for home consumption. Specifically excluded from the definition of food for home consumption are alcoholic beverages, tobacco and prepared hot foods sold for immediate consumption, e.g., delicatessen items and items from in-store snack bars.

In essence, this means that a quart of milk will not be taxable if sold in a "retail food store" but will be taxable if sold in a store that does not qualify as a retail food store; moreover, non-food items such as household cleansers and paper products will continue to be taxed even when sold in a retail food store.

Tax on Medical Services

The deduction for health care practitioners applies to receipts from payments to a health care practitioner by a managed health care provider or health care insurer if the payments are for non-Medicaid managed care services provided pursuant to a contract. To qualify for the deduction, the services must be within the scope of practice of the health care practitioner providing the services. Health care practitioners eligible for the deduction are divided into 14 categories of licensed health care professionals,

Tax on Food and Medical Services (Cont.)

including physicians, nurses, osteopaths, dentists, chiropractors, optometrists, podiatrists, psychologists and various therapists.

The new gross receipts tax deductions for food and certain health care services will result in a reduction in the gross receipts tax base for municipalities and counties. That loss of municipal and county gross receipts tax revenue will be reimbursed by the state through new distributions to local governments. The cost of the new deductions to the general fund are offset by the repeal of a one-half percent credit, known as the municipal credit, which taxpayers in municipalities have used to remain competitive with businesses in unincorporated county areas. The municipal credit previously reduced the gross receipts tax revenue retained by the state to 4.5 percent. Repeal of the municipal credit will result in a tax increase for purchases of goods and services from businesses located in municipalities.

High-Wage Jobs Tax Credit

Laws 2004, Chapter 15 provides that an employer that has more than 50 percent of its sales outside New Mexico and that is eligible for in-plant training assistance may claim a tax credit equal to 10 percent of wages and benefits paid to new employees in "high-wage" jobs.

An eligible high-wage job must pay at least $40,000 per year if located in a municipality with a population of 40,000 or more or at least $28,000 per year if located elsewhere. Also, the job must have been occupied for at least 48 weeks prior to claiming the credit. The maximum credit is $12,000 per year per employee.

As of May 2004, the New Mexico Labor Department reports that the statewide median annual wage is $24,370. The median annual wages for the metropolitan statistical areas are: Santa Fe, $29,180; Albuquerque, $25,820; and Las Cruces, $21,060.

Motor Vehicle Excise Exemption

Beginning July 1, 2004 and continuing for five years, gasoline-electric hybrid motor vehicles will be exempt from the three percent motor vehicle excise tax.

Nursing Home Bed Surcharge

Laws 2004, Chapter 4 imposes a flat rate daily bed surcharge that is the equivalent of six percent on the gross receipts of services provided by licensed nursing homes, licensed intermediate care facilities and residential treatment centers. The increased revenue could help the state obtain additional federal matching funds.

To offset the increased cost to non-Medicaid patients resulting from the daily bed surcharge, a refundable income tax credit of $10.00 per day was created.

In May 2004, the federal Centers for medicare and Medicaid Services notified the New Mexico Human Services Department that the bed surcharge might not qualify for federal matching funds because it might constitute an impermissible provider tax due to the passage of the refundable income tax credit. The Human Services Department responded that the surcharge does not constitute an impermissible provider tax because health care facilities are considered to be the taxpayers under the regulations, while it is individuals occupying the beds who are eligible for the tax credit. Whether or not Medicaid funding will be available to reimburse facilities for the cost of the new tax is unresolved at the time of this writing; however, the bed tax went into effect on July 1, 2004.

Regional Transit Tax

Laws 2004, Chapter 17 authorizes a municipal and county regional transit gross receipts tax for management, construction or operation of a public transit system. Subject to voter approval, a municipality or county may impose the tax in increments of one-sixteenth percent up to a maximum of one-half percent.

A Regional Transit District (RTD) may be formed by two or more municipalities or counties by signing a contract that conforms to the Regional Transit District Act (Laws 2003, Chapter 65). At present, two RTDs are in the process of forming. The North Central RTD will include Santa Fe, Los Alamos and Rio Arriba counties, and the Mid Region RTD is in the Albuquerque area.

County Local Option Tax

All counties are authorized to levy an additional one-sixteenth percent gross receipts tax by Laws 2004, Chapter 110. The revenue may be used for general purposes. In addition, this legislation creates an "optional referendum selection" process. This means that the governing body of a county may choose whether to put the tax increase before the voters in an election. If the body chooses to impose the tax without voter approval, voters have the right to force an election by petition.

Finally, this legislation authorizes all counties to impose the correctional facility gross receipts tax (one-eighth percent). Previously, only Chaves, Dona Ana and Valencia counties were authorized to impose this tax. The legislation permits the proceeds from the correctional facility gross receipts tax to be used for operational and capital expenditures.

With this legislation, the potential total county gross receipts tax is 1.375 percent, excluding certain taxes that are specific to individual counties.

Insurance Premium Tax

The base tax rate imposed on the value of insurance premiums is 3.003 percent. This tax applies to all risk policies written in New Mexico. Laws 2004, Chapter 122 imposes a new one-percent surcharge on premiums associated with health insurance, including health maintenance organizations and nonprofit health care plans. The surcharge became effective July 1, 2004.

Military Base Retention Tax Deduction

Laws 2004, Chapter 16 provides a compensating tax deduction for military research and development activities. The deduction is for the value of test articles when the research or testing service is performed under contract to the United States Department of Defense. The value of property purchased by a prime contractor who operates a national laboratory is excluded. The deduction is intended to help attract defense system testing contracts, such as the "Future Combat System and Advanced Tactical Laser Weapons System" programs at White Sands Missile Range.

Governmental Gross Receipts Taxation Expansion

Laws 2004, Chapter 69 expands the types of government revenue that are subject to the governmental gross receipts tax. Receipts from vehicle parking fees, aircraft tie-down fees and boat docking fees are added to the definition of "governmental gross receipts tax". In 2003, the Blue Ribbon Tax Reform Commission included this expansion as one of its recommendations to the 2004 legislature. Seventy-five percent of the revenue from this source is utilized by the New Mexico Finance Authority to pay for public improvement projects. In fiscal year 2005, an estimated 139 projects totaling over $200 million have been authorized by the legislature.

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